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IN THE

Supreme Court of the United States

October Term, 1959.

No. 890

POWERS MANUFACTURING CO., INC.,

Petitioner,

vs.

ALL-STEEL EQUIPMENT INC.,

Respondent.

Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

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SUBJECT INDEX

PAGE

Jurisdiction 2

Question presented 2

Constitutional provision and state statute involved 3

Statement of the case 4

Argument 7

I.

The decision of the Court of Appeals for the Ninth Circuit of which this petition seeks review adds to the conflict of decisions on the question presented herein, and this court should settle the conflict 7

II.

The question presented is important and if it be a question of federal law it is one which has not been, but should be settled by the Supreme Court of the United States 12

III.

The Court of Appeals for the Ninth Circuit has decided an important state question in a way in conflict with applicable state law 13

IV.

The Court of Appeals for the Ninth Circuit in the case at bar sanctioned a departure by the District Court so far from the accepted and usual course of judicial proceedings as to violate the Fifth Amendment to the Constitution and to call for an exercise of the Supreme Court's power of supervision 14

Appendix:

Opinion of the United States Court of Appeals, Ninth Circuit ..... App. p. 1

Judgment ..... App. p. 8

TABLE OF AUTHORITIES CITED

CASES — PAGE

Air King Products Co. v. Hazeltine Research, 94 Fed. Supp. 85, 87 U. S. P. Q. 315 8

American Street Car v. Jones, 122 Fed. 803 10

Armstrong v. Shell Co., 98 Cal. App. 769, appeal declined 98 Cal. App. 769 ..... 11, 13, 14

Automatic Radio v. Hazeltine Research, 176 F. 2d 799, aff'd 339 U. S. 827 9

Brown v. Lapham, 27 Fed. 77 11

Bucky v. Sebo, 208 F. 2d 304 10

Crew v. Flanagan, 102 U. S. P. Q. 324 10

Dall Motor Parts Co. v. Packard, 124 Ohio St. 363, 178 N. E. 835, 12 U. S. P. Q. 185 7

Drackett Chemical v. Chamberlain, 63 F. 2d 853 10

Eastern States Petroleum Co. v. Universal Oil Co., 22 Del. Ch. 333, 2 A. 2d 138, 37 U. S. P. Q. 834 7

Elgin National Watch Co. v. Bulova Watch Co., 93 U. S. P. Q. 391, 94 U. S. P. Q. 218 8

Eskimo Pie Corp. v. National Ice Cream, 20 F. 2d 1003 11

Hardwicke v. Galbraith, 147 Pa. 333 8

Harlow v. Putnam, 124 Mass. 553 10

Hazeltine Research v. DeWald, 276 App. Div. 1001, 95 N. Y. S. 2d 772, 85 U. S. P. Q. 222, rvrs'ng 84 N. Y. S. 2d 597, 79 U. S. P. Q. 446 8

Heller Inc. v. Lassner Co., 214 App. Div. 315, 212 N. Y. Supp. 175 7

Holmes v. McGill, 108 Fed. 238 10

Jungersen v. Morris Kaysen, 95 U. S. P. Q. 162, aff'd 173 Pa. Super. 114, 97 U. S. P. Q. 244 8

K-W Ignition v. Unit Coil, 93 Ohio St. 128, 112 N. E. 199 10

Lathrop v. Rice, 17 Fed. Supp. 622 11

PAGE

Marston v. Swett, 66 N. Y. 206 10
Martin v. New Trinidad Lake Asphalt, 255 Fed. 93 10
Mudgett v. Thomas, 55 Fed. 645 10
Pope Mfg. v. Owsley, 27 Fed. 100 11
Ross v. Dowden Mfg. Co., 147 Iowa 180, 123 N. W. 182 11
Ross v. Fuller & Warren Co., 105 Fed. 510 10
St. Paul Plow Works v. Starling, 140 U. S. 196, 11 S. Ct. 803, 35 L. Ed. 404 9
Schutte & Koerling v. Wheeler Co., 295 Fed. 158 10
Skidmore v. Fahys Watch Case, 28 App. Div. 94, 50 N. Y. Supp. 1016 10
Skinner v. Wood, 140 N. Y. 217, 35 N. E. 491 10
Universal Rim Co. v. Scott, 21 F. 2d 346 7
Vicki Hosiery v. Margulies, 164 Fed. Supp. 738, 118 U. S. P. Q. 534 7
Washburn & Moen Mfg. Co. v. Cincinnati Barbed-Wire Fence, 22 Fed. 712 7
White v. Lee, 14 Fed. 789 11

STATUTES

California Civil Code, Sec. 1689 ..... 3, 13
United States Code, Title 28, Sec. 1254 2
United States Code, Title 28, Sec. 1332 4
United States Constitution, Fifth Amendment 2, 3, 14

IN THE

Supreme Court of the United States

October Term, 1959.

No. .....

BOWERS MANUFACTURING CO., INC.,

Petitioner,

vs.

ALL-STEEL EQUIPMENT INC.,

Respondent.

Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

To the Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Your Petitioner, Bowers Manufacturing Co., Inc., a corporation, respectfully prays that a writ of certiorari issue to review the Judgment of the United States Court of Appeals [R. p. 138], reported at 124 U. S. P. Q. 352, not yet appearing in Federal Reporter, copy appended hereto.

The grounds upon which certiorari is sought are:

I. The decision of the Court of Appeals for the Ninth Circuit, of which this petition seeks review, adds to the conflict of decisions on the question presented herein, and this Court should settle the conflict.

II. The question presented is important and if it be a question of federal law it is one which has not been,

but should be settled by the Supreme Court of the United States.

III. The Court of Appeals for the Ninth Circuit has decided an important state question in a way in conflict with applicable state law.

IV. The Court of Appeals for the Ninth Circuit in the case a bar sanctioned a departure by the District Court so far from the accepted and usual course of judicial proceedings as to violate the Fifth Amendment to the Constitution and to call for an exercise of the Supreme Court's power of supervision.

Jurisdiction.

The aforesaid judgment of the Court of Appeals for the Ninth Circuit was dated and entered January 29, 1960. No rehearing was sought or had. Statutory jurisdiction is conferred on this Court by Title 28, United States Code, Section 1254. Citations of the numerous conflicting decisions on the question involved are contained in the section denoted ARGUMENT.

Question Presented.

The Judgment of the Court of Appeals for the Ninth Circuit raises the following question of law:

May a licensee effectively rescind a patent license, entered into after being notified of infringement, in the absence of a provision in the license affirming such right of termination; on the ground of failure of consideration based upon discovered (but not adjudicated) invalidity of the licensed patent; and when sued on the rescinded license after the licensee has stood out from under the protection of said patent, offer proof of invalidity as a defense to the suit?

Constitutional Provision and State Statute Involved.

The pertinent part of the Constitution of the United States involved is the Fifth Amendment set out below:

"No person shall be * * * deprived of life, liberty, or property, without due process of law; * * *."

The pertinent section of the California Civil Code states in section 1689:

"A party to a contract may rescind the same in the following cases only:

"1. If the consent of the party rescinding, or of any party jointly contracting with him was given by mistake, or obtained through duress, menace, fraud, or undue influence, exercised by or with the connivance of the party as to whom he rescinds, or of any other party to the contract jointly interested with such party;

"2. If, through the fault of the party as to whom he rescinds, the consideration for his obligation fails, in whole or in part;

"3. If such consideration becomes entirely void from any cause;

"4. If such consideration before it is rendered to him fails in a material respect from any cause;

"5. By consent of all the other parties; or

"6. Under the circumstances provided for in sections 1785 and 1789 of this code (Enacted 1872. As amended Stats. 1931, c. 1070, p. 2260; §10.)"

Statement of the Case.

This is an action for specific performance of a patent license agreement heretofore entered into between the Respondent and Petitioner.

The District Court had original jurisdiction on diversity of citizenship between the parties and an amount in controversy exceeding the then requirement of Three Thousand Dollars ($3,000.00), exclusive of interest and costs by virtue of 28 United States Code, Section 1332.

As of January 1, 1955, Respondent and Petitioner entered into a nonexclusive license agreement [R. pp. 30-40] under which Petitioner was licensed to make, use and sell certain devices under the Keierleber Patent No. 2,424,829 owned by Respondent, and was required to render periodic financial statements and pay royalties to Respondent.

Petitioner duly performed all of the terms and conditions of said license agreement on its part to be performed until it obtained facts upon which a conclusion was reached that the licensed patent was invalid, whereupon Petitioner gave prompt notices [R. pp. 80-84] of its claim of invalidity of said patent and failure of consideration for said agreement and rescinded, denounced and abandoned said license agreement, stating that it regarded itself as a stranger to the patent, and not shielded by the agreement from a suit for patent infringement. In and by said notices, Petitioner demanded that monies theretofore paid by it to Respondent be restored to it.

Respondent's complaint alleging default and praying for an accounting and payment of royalties was filed on April 11, 1958 [R. pp. 3-6]. Petitioner in answer thereto set out specific denials and also certain affirmative defenses based on (1) failure of consideration under said license agreement; (2) rescission of said license agreement; and (3) estoppel and laches [R. pp. 6-11].

Petitioner's answer was accompanied by a counterclaim for restoration of royalties previously paid, confirmation of its rescission of the contract, and for declaratory relief declaring the patent invalid and void and not infringed by Petitioner [R. pp. 11-18].

Respondent moved [R. pp. 79-80] to strike out Petitioner's specific denial that any valid license agreement existed between the parties and also Petitioner's affirmative averral that the license agreement which formerly existed between the parties had been rescinded, denounced, abandoned and terminated by the Petitioner.

Respondent also moved to strike Petitioner's affirmative defenses of failure of consideration, rescission, and estoppel and laches.

Respondent further moved to dismiss Petitioner's counterclaim.

The foregoing motions were granted, and a Minute Order, without opinion, was entered July 15, 1958 [R. pp. 84-85]. A formal Order Striking Portions of Defendant's Answer and Dismissing Defendant's counterclaim was dated and filed July 18, 1958 [R. pp. 85-87].

The Petitioner appealed from this Order to the United States Court of Appeals for the Ninth Circuit, [R. p. 87] being case No. 16152.

After briefs were submitted and oral argument had, the Court of Appeals for the Ninth Circuit dismissed the appeal as being from an unappealable order [R. p. 129a].

After remand Respondent file a Motion for Summary Judgment [R. p. 106] in the District Court, which was granted, and Findings of Fact and Conclusions of Law and Judgment [R. pp. 110-115] dated May 27, 1959, were filed and entered that date in favor of Respondent.

The Petitioner then appealed from such Judgment to the United States Court of Appeals for the Ninth Circuit [R. p. 116], being case No. 16527.

After briefs and oral argument, the Court of Appeals for the Ninth Circuit rendered an opinion dated January 29, 1960, affirming the Judgment of the District Court. The opinion may be found beginning at page 132 of the Record, a copy is printed as an appendix to this petition. It is reported at 124 U. S. P. Q. 352, but has not yet appeared in the Federal Reporter. Judgment predicated upon the opinion, dated January 29, 1960 was filed and entered that date [R. p. 138].

ARGUMENT.

I.

The Decision of the Court of Appeals for the Ninth Circuit of Which This Petition Seeks Review Adds to the Conflict of Decisions on the Question Presented Herein, and This Court Should Settle the Conflict.

There are so many decisions involved, in a hopeless confusion of cases holding directly opposite on similar sets of facts, that rather than quote or discuss them in detail, we deem it more useful to this Court to present them in tabulated form.

1. Cases involving nonexclusive licenses where:

Repudiation Was Approved.	*Repudiation Was Disapproved.*
Universal Rim Co. v. Scott, N. D. Ohio E. D., 1922, 21 F. 2d 346;	*Washburn & Moen Mfg. Co. v. Cincinnati Barbed-Wire Fence*, C. C. S. D. Ohio, 1884, 22 Fed. 712;
Vicki Hosiery v. Margulies, E. D. Pa., 1958, 164 Fed. Supp. 738, 118 U. S. P. Q. 534.	*Dall Motor Parts Co. v. Packard* 1931, 124 Ohio St. 363, 178 N. E. 835, 12 U. S. P. Q. 185;
	Eastern States Petroleum Co. v. Universal Oil Co., 1938, 22 Del. Ch. 333, 2 A. 2d 138, 37 U. S. P. Q. 834;
	Heller Inc. v. Lassner Co. (1st Dept. 1925), 214 App. Div. 315, 212 N. Y. Supp. 175;

Repudiation Was Approved.	*Repudiation Was Disapproved.*
	Hazeltine Research v. DeWald (1st Dept. 1950), 276 App. Div. 1001, 95 N. Y. S. 2d 772, 85 U. S. P. Q. 222, reversing 84 N. Y. S. 2d 597, 79 U. S. P. Q. 446;
Elgin National Watch Co. v. Bulova Watch Co. (N. Y. Sup. Ct. 1952), 93 U. S. P. Q. 391, 94 U. S. P. Q. 218 (while this case found that facts did not support repudiation, the court did affirm the principle);	
	Jungersen v. Morris Kaysen (Pa. C. P. 1952), 95 U. S. P. Q. 162, aff'd 173 Pa. Super. 114, 97 U. S. P. Q. 244 (1953);
	Hardwicke v. Galbraith, 147 Pa. 333;
	Air King Products Co. v. Hazeltine Research, E. D. N. Y. 1950, 94 Fed. Supp. 85, 87 U. S. P. Q. 315.

There are two Supreme Court cases which some authorities on the subject of repudiation might classify as falling under the column "Repudiation was disapproved" referring to nonexclusive licenses, and which Petitioner believes involve facts not found in the present case. The

two cases in question are *St. Paul Plow Works v. Starling*, 1891, 140 U. S. 196, 11 S. Ct. 803, 35 L. Ed. 404, and *Automatic Radio v. Hazeltine Research*, 1st Cir. 1949, 176 F. 2d 799, aff'd 339 U. S. 827 (1950).

In the *St. Paul Plow v. Starling* case, *supra*, the facts indicate defendant rescinded the patent license by written notice upon the ground that the construction of the plow under plaintiff's patent was unsatisfactory, that a large number of the completed plows had been returned to defendant as unserviceable and that in the future defendant would manufacture a plow of its own design. Further, the question of invalidity of the licensed patent came up for the *first time* at the trial, when defendant was sued for royalties. The Supreme Court through Mr. Justice Blatchford affirmed the lower court's decision in favor of plaintiff and held that rescission was not proper in that case.

In *Automatic Radio v. Hazeltine Research, supra*, the Court of Appeals for the First Circuit did not allow repudiation. But, the court did recognize that in some cases unilateral repudiation by a licensee is possible where the stringent requirements for repudiation are met. The facts indicated that licensee did not attempt to repudiate until *after* the complaint had been filed. The Supreme Court through Mr. Justice Minton did not discuss the specific repudiation referred to in the Court of Appeals' decision, 176 F. 2d 799, 809, but only discussed the challenging of validity of the licensed patent which was raised for the *first time* by defendant licensee at the time of trial.

In the present case Petitioner repudiated the license on grounds of invalidity of the licensed patent *far in advance* of the action brought by Respondent. The facts of the above two Supreme Court cases differ from the

present facts and the law in those cases therefore, is neither controlling nor applicable here.

2. Cases involving exclusive licenses where:

Repudiation Was Approved.

Mudgett v. Thomas, C. C. S. D. Ohio, 1893, 55 Fed. 645;

Ross v. Fuller & Warren Co., C. C. N. D. N. Y. 1900, 105 Fed. 510;

Drackett Chemical v. Chamberlain, 6th Cir. 1933, 63 F. 2d 853;

Martin v. New Trinidad Lake Asphalt (D. C. N. J. 1919), 255 Fed. 93 (while this case found that facts did not support repudiation, the court did affirm the principle);

Schutte & Koerling v. Wheeler Co., D. C. E. D. Pa. 1924, 295 Fed. 158;

Harlow v. Putnam, 1878, 124 Mass. 553;

Bucky v. Sebo, C. A. 2, 1953, 208 F. 2d 304 (contains dicta that repudiation removes estoppel);

Crew v. Flanagan, 1954, Minn. Sup. Ct., 102 U. S. P. Q. 324.

Repudiation Was Disapproved.

Holmes v. McGill (2nd Cir. 1901), 108 Fed. 238. (But see contrary dicta in recent CA 2 case cited in opposite column, *Bucky v. Sebo, supra.*)

American Street Car v. Jones (C. C. N. D. N. Y., 1903), 122 Fed. 803;

Skinner v. Wood, 1893, 140 N. Y. 217, 35 N. E. 491;

Marston v. Swett, 1876, 66 N. Y. 206;

Skidmore v. Fahys Watch Case (1st Dept. 1898), 28 App. Div. 94, 50 N. Y. Supp. 1016;

K-W Ignition v. Unit Coil, 1915, 93 Ohio St. 128, 112 N. E. 199.

3. Cases involving licenses wherein the decisions do not indicate what type of license was involved where:

Repudiation Was Approved.

Brown v. Lapham, 1886, C. C. S. D. N. Y., 27 Fed. 77;

Lathrop v. Rice, 1936, D. C. W. D. N. Y., 17 Fed. Supp. 622 (facts did not show compliance with requirements for repudiation, but court did set forth with approval grounds upon which repudiation may be allowed);

Ross v. Dowden Mfg. Co., 1909, 147 Iowa 180, 123 N. W. 182;

Armstrong v. Shell Co., 1929, 98 Cal. App. 769. Cal. Supreme Court declined to hear appeal, 98 Cal. App. 769, 784.

Repudiation Was Disapproved.

Pope Mfg. v. Owsley, 1886, C. C. N. D. Ill., 27 Fed. 100;

White v. Lee, 1882, C. C. D. Mass., 14 Fed. 789 (held for licensee, but on other grounds);

Eskimo Pie Corp. v. National Ice Cream, 1927, D. C. W. D. Ky., 20 F. 2d 1003 (dicta only, facts showed an acquiescence to contract cancellation).

Cases in this section apparently reflect indifference on the part of the deciding court as to whether the license in issue is exclusive or nonexclusive, otherwise the type of license would have been identified.

The above listed cases are fairly representative of the conflict and confusion of law on the question posed to this Court.

While we have segregated the cases into three categories, it is Petitioner's position that the type of license should not be controlling, but that repudiation is proper whenever discovery is made that the licensed patent is invalid, and the licensee should have the right to attack validity as a defense in a suit on the repudiated license.

II.

The Question Presented Is Important and if It Be a Question of Federal Law It Is One Which Has Not Been, but Should Be Settled by the Supreme Court of the United States.

We doubt that the question is one of federal law but this point is submitted as an alternative due to the remark of Judge Barnes in his opinion in the present case that one of the oldest doctrines of the *patent law* is well established that a licensee cannot attack the validity of his licensor's patent. We do not think that Judge Barnes was referring to the federal statutes on the subject of patent law but rather to the identification of a field of law.

In any event the question is an important one because the public indirectly pays a tribute to patentees by reason of the royalties paid by a licensee, and it is a matter of common knowledge that the licensing of patents on a royalty basis is widespread in industry.

III.

The Court of Appeals for the Ninth Circuit Has Decided an Important State Question in a Way in Conflict With Applicable State Law.

We think that the question posed, being one of contract law, is a state question. Many of the cases cited above were tried and appealed in state courts. In the present case jurisdiction of the federal court was available only because of diversity of citizenship and the requisite jurisdictional amount.

The question is important not only in the State of California but in all of the other states of the Union and has arisen in many of the other states. It is important to the public for the same reasons as discussed under Point II.

The California state law involved has two facets: First, the codification, and second, the controlling decided case, *Armstrong v. Shell, supra,* 98 Cal. App. 769.

The codification applicable here is California Civil Code, Section 1689, *supra.* This code section is referred to in the opinion of the Court of Appeals for the Ninth Circuit but is rejected as providing a vehicle for rescission but not "an additional substantive basis therefor". We submit that this is an erroneous interpretation. The quoted provision of the Civil Code of California, *supra,* is substantive law, as distinguished from procedural law found in the California Code of Civil Procedure.

The other phase of the present point is that the California District Court of Appeal decided in *Armstrong v. Shell, supra,* that a licensee may rescind and repudiate a

license upon discovery of invalidity of the licensed patent and attack the validity of the patent. The opinion does not show and no point is made as to whether the license was exclusive or nonexclusive. It is therefore to be concluded that under the California decision it makes no difference whether the license is exclusive or nonexclusive. That decision became the law of the State by reason of the Supreme Court of California declining to take the case on appeal.

The decision of the Court of Appeals for the Ninth Circuit in the present case is clearly and unequivocably in conflict with the applicable law of the State of California as defined in *Armstrong v. Shell, supra.*

IV.

The Court of Appeals for the Ninth Circuit in the Case at Bar Sanctioned a Departure by the District Court so Far From the Accepted and Usual Course of Judicial Proceedings as to Violate the Fifth Amendment to the Constitution and to Call for an Exercise of the Supreme Court's Power of Supervision.

Under the Fifth Amendment *supra*, a litigant is entitled to his "day in court" as one of the guarantees under "due process of law".

There was no clause in the license agreement [R. pp. 36-40] prohibiting petitioner from questioning the validity of the patent under which petitioner was licensed. Consequently after the license terminated there was nothing to prevent petitioner from attacking the patent. Under the Civil Code of California petitioner had a right to

repudiate and rescind its contract and treat itself as a stranger to the patent. As a stranger to the patent petitioner should have a right to defend any action involving either the patent or royalties and to present a counterclaim for declaratory relief in the circumstances.

The District Court by granting respondent's motion to strike the vital defenses pleaded in the answer and concurrently dismissing the counterclaim, deprived petitioner of its "day in court" and such constituted a departure sanctioned by the Court of Appeals for the Ninth Circuit.

Respectfully submitted,

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Los Angeles, California, April 6, 1960.

APPENDIX

Opinion of the United States Court of Appeals, Ninth Circuit.

Bowers Manufacturing Co., Inc., a Corporation Appellant, vs. All-Steel Equipment Inc., a Corporation, Appellee. *No. 16,527. Jan. 29, 1960.*

On Appeal from the United States District Court for the Southern District of California, Central Division.

Before: Barnes, Hamley and Hamlin, Circuit Judges.

Barnes, Circuit Judge:

This is an action for specific enforcement of a patent license agreement. Summary judgment was granted to plaintiff All-Steel, and from this judgment Bowers presses this appeal. The district court had jurisdiction of this action. 28 U. S. C. §1332. This Court has jurisdiction on appeal. 28 U. S. C. §1291.

As of January 1, 1955, appellee entered into a non-exclusive license agreement with appellant, under which appellant was licensed to make, use and sell certain devices under the Keierleber Patent; was required to render certain financial statements; and pay periodic royalties to appellee. This agreement was the culmination of an amicable exchange of letters in which the subject of possible infringement was discussed.

On December 14, 1956, appellant decided that the patent was invalid, purported to rescind the agreement, and demanded the return of money previously paid as royalties. No further payment of royalties was made. Thereafter, appellee filed a complaint for specific performance. Appellant answered, (1) denying that the license agreement still existed; (2) alleging consideration had failed under

the license agreement; (3) alleging the license agreement had been rescinded; and (4) alleging estoppel and laches. Appellant further counterclaimed for restoration of royalties paid, and for declaratory relief. Appellee's motion to strike all the defenses and counterclaims was granted. Appellant appealed from this order, but the appeal was dismissed as being from an unappealable order. After remand, a summary judgment was granted on the pleadings plus some interrogatories which established the amount of royalties due under the license. The judgment provided for payment of royalties accrued, and contained a mandatory injunction ordering future rendition of financial reports and payment of royalties.

It was stipulated by the parties (and the stipulation approved by this Court) that the same briefs filed in the dismissed appeal be used on this appeal. The question presented on this appeal is the legal sufficiency of the defenses and counterclaims ordered stricken by the trial court. In other words, can a licensee of a nonexclusive license attack the validity of his licensor's patent?

We note first that the purported rescission of the license by Bowers was unequivocal in nature.[1]

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[1] "We hereby rescind, denounce, and abandon said license agreement, on the ground that said patent is and always has been invalid, and therefore, is and always has been, void as consideration to support said agreement. We now regard ourselves as strangers to said patent, not shielded by said agreement from a suit for patent infringement.

"We call upon you to restore to us the monies heretofore paid under said agreement, and hereby offer to stand as strangers to said patent, continuously from the beginning of said license, nunc pro tunc."

"One of the oldest doctrines of the patent law,"[2] the general rule, is well established that a licensee cannot attack the validity of his licensor's patent. United States v. Harvey Steel Co., 1905, 196 U. S. 310; Kinsman, *et al.* v. Parkhurst, 1855, 59 U. S. (18 How.) 289. It is contended that this is even more true with a nonexclusive license, as in the instant case, than in the case of an exclusive license. A reading of the cases shows most courts seem to be indifferent as to the nature of the license involved. Whether it is exclusive or nonexclusive is usually ascertained by some chance remark of the court. Cases dealing with both types of licenses are cited indiscriminately. But logic would indicate that a different treatment is justified. The two types of agreements differ basically because the consideration inducing them differs in each. In an exclusive license the monopoly values of the patent loom large. The license is in effect a grant of the patent. But a nonexclusive license cannot eliminate competition. It constitutes little more than a shield from suit for infringement by the grantor. Thus questionable validity of the patent cannot constitute a failure of consideration.

Appellant contends that there is, or should be, an exception to the general rule when the nonexclusive licensee unilaterally and unequivocally rescinds the license *prior* to the action for specific performance of the license. Its reasoning is that since the license has been rescinded and is no longer in existence, the licensee is no longer precluded from attacking the validity of the patent. Appellant therefore contends that an issue of fact must be tried,

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[2]MacGregor v. Westinghouse, 1947, 329 U. S. 402, 408 (dissenting opinion).

i.e., a determination of the effectiveness of the purported rescission. Since the rescission is based on failure of consideration by reason of the invalidity of the patent, the validity of the patent becomes an issue in the lawsuit.

It is undisputed that a nonexclusive licensee cannot attack the validity of the licensor's patent for the first time during the lawsuit for royalties, unless illegal price fixing provisions are inseverable from the royalty clauses. Automatic Radio Co. v. Hazeltine, 1950, 339 U. S. 827; Katzinger Co. v. Chicago Mfg. Co., 1947, 329 U. S. 394; Mac Gregor v. Westinghouse Co., 1947, 329 U. S. 402; United States v. Harvey Steel Co., *supra*.

Nor can advance repudiation on the basis of nonuser be effective to end the license. St. Paul Plow Works v. Starling, 1891, 140 U. S. 184; Heath v. A. B. Dick Co., 7 Cir., 1958, 253 F. 2d 30. Even when government regulations require cessation of use, an advance repudiation is ineffective. Ohio Citizens Trust v. Air-Way Electric App. Corp., N. D. Ohio, 1944, 56 F. Supp. 1010.

It seems to be conceded by appellee that advance repudiation of an *exclusive* license for invalidity will allow the licensee to attack the validity of the patent at the suit for royalties. Martin v. New Trinidad Lake Asphalt Co., (D. N. J. 1919) 255 Fed. 93; Crew v. Flanagan, 1954, 242 Minn. 549, 65 N. W. 2d 878. And appellant urges that the same rule should apply where there has been an attempted rescission for failure of consideration by reason of invalidity of the patent by a nonexclusive licensee *prior to the suit for royalties*. He relies on two district court cases: Viki Hosiery Corp. v.

Margulies, E. D. Pa., 1958, 164 F. Supp. 738,[3] and Universal Rim Co. v. Scott, N. D. Ohio, 1922, 21 F. 2d 346.[4]

Despite the holdings of these cases, there remains the question, should repudiation prior to suit be such a significant difference that it allows a licensee in effect to attack the validity of his licensor's patent contrary to the general rule? It is difficult to see why a procedural technicality such as this should create substantive rights in a licensee.

In many cases, part of the consideration for entering a license agreement is the dismissal with prejudice of a pending infringement suit, or the failure to file such a proposed suit. Were either such the case, it seems clear that invalidity of the patent could not constitute failure of consideration for a nonexclusive license. It is true that here there was not even the threat of an infringement action, and it would seem that consideration is more closely connected with the validity of the patent. However, this raises an issue of adequacy, rather than failure of consideration.

"Once a contract is supported by consideration, its terms are up to the parties. Whether the consideration is adequate or not is no concern of the court. Restatement of Contracts, §81. The parties are free to fix their own terms, and they have done so here."

Warner-Lambert Co., Inc. v. Reynolds, Inc., S. D. N. Y., 1959, 123 U. S. P. Q. 431, 439.

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[3]This is a pleading case, and does not go into the substantive law.

[4]In the Universal Rim case, the rights of the parties were complicated by the intervention of a receivership, and his rights with respect to an executory contract.

Appellant makes a separate argument based on §1689 of the California Civil Code which provides for rescission for failure of consideration.[5] This begs the overriding question of whether invalidity of the patent is in fact failure of consideration. The California Civil Code section provides a vehicle for rescission, but not an additional substantive basis therefor. Appellee argues that appellant has at most made a mistake of law regarding the validity of the patent, and that rescission is never available for mere mistake of law.

General policy considerations favoring settlement of disputes and litigation by means of such nonexclusive licenses should not allow a licensee to attack the validity of a licensor's patent by means of a device such as prior rescission, anymore than by direct attack through a suit for royalties. The licensee has bought temporary peace by agreeing to the license, and should be required to abide by his bargain. The agreement itself provides sufficient

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[5]California Civil Code § 1689 provides:
"*Grounds*

"A party to a contract may rescind the same in the following cases only:

"1. If the consent of the party rescinding, or of any party jointly contracting with him was given by mistake, or obtained through duress, menace, fraud, or undue influence, exercised by or with the connivance of the party as to whom he rescinds, or of any other party to the contract jointly interested with such party;

"2. If, through the fault of the party as to whom he rescinds, the consideration for his obligation fails, in whole or in part;

"3. If such consideration becomes entirely void from any cause;

"4. If such consideration before it is rendered to him fails in a material respect, from any cause;

"5. By consent of all the other parties, or

"6. Under the circumstances provided for in sections 1785 and 1789 of this code. (Enacted 1872. As amended Stats. 1931, c. 1070, p. 2260, § 10.)"

means of termination. Appellant may cancel if: (a) the Keierleber Patent is held invalid by a court of competent jurisdiction; (b) appellant completely discontinues manufacture and sale of boxes covered by the patent. These conditions would allow cancellation if the license became unduly oppressive to appellant. Since neither of these events has occurred, appellant should be held to its contract and estopped to deny the validity of the licensor's patent under a nonexclusive license agreement. Muth v. J. W. Speaker Corp. 7 Cir., 1959, 262 F. 2d 797; Heath v. A. B. Dick Co., *supra;* Automatic Radio Mfg. Co. v. Hazeltine Research, 1 Cir., 1949, 176 F. 2d 799 *affirmed,* 339 U. S. 827; Ellis: Patent Licenses, 3rd ed., 1958, Ch. XXVI.

At the time of oral argument in this case we suggested that counsel furnish additional briefs on appellant's right, as a licensee, to attack the validity of its licensor's patent by means of a suit for declaratory relief.

Any standing which appellant might have to pray for declaratory relief must be founded in the license, and the infringement controversy which that license settled. We have held *supra* that appellant may not seek to avoid its contractual responsibilities by rescission prior to the institution of the action for royalties. The same reasons apply with equal force to any attempt to do so by means of declaratory judgment. Appellant has no more right to attack its licensor's patent in a declaratory action than by rescission, or in defense of a suit for royalties.

The judgment is *affirmed.*

(Endorsed) Opinion Filed Jan. 29, 1960.

Frank H. Schmid, Clerk.

United States Court of Appeals for the Ninth Circuit.

Bowers Manufacturing Co., Inc., a Corporation, Appellant, vs. All Steel Equipment, Inc., a Corporation, Appellee. No. 16,527.

Judgment.

Appeal from the United States District Court for the Southern District of California, Central Division.

This cause came on to be heard on the Transcript of the Record from the United States District Court for the Southern District of California, Central Division, and was duly submitted.

On consideration whereof, it is now here ordered and adjudged by this Court, that the Judgment of the said District Court in this cause be, and hereby is affirmed.

(ENDORSED) Judgment
Filed and entered: January 29, 1960

Frank H. Schmid, Clerk.

FILE COPY

FILED
MAY 24 1960
JAMES R. BROWNING, Clerk

IN THE

Supreme Court of the United States

OCTOBER TERM, 1959.

No. 890

BOWERS MANUFACTURING CO., INC.,

Petitioner,

vs.

ALL-STEEL EQUIPMENT INC.,

Respondent.

RESPONSE TO PETITION FOR WRIT OF CERTIORARI.

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INDEX

PAGE

Statement of Fact 1

Question Presented 4

Argument 5

1. The Decision of the Court of Appeals in this Case is in Harmony with the Decision of this Court and with the Decisions of Other Courts of Appeal. There is no Basic Conflict of Decision. 9

2. The Opinion Below is not in Conflict with Applicable State Law. 13

Conclusion 15

Authorities Cited

Air King Products Co. v. Hazeltine Research, E.D. N.Y. 1950, 94 Fed. Supp. 85, 87 U.S.P.Q. 315 11

Automatic Radio Mfg. Co., Inc. v. Hazeltine Research, Inc., 176 F.2d 799 (C.A. 1, 1949; affirmed 339 U.S. 827) 6, 8, 9

Dall Motor Parts Co. v. Packard, 1931, 124 Ohio St. 363, 178 N.Ed. 835, 12 U.S.P.Q. 185 11

Del Riccio et al. v. Photochart, 268 P.2d 814 14

Eastern States Petroleum Co. v. Universal Oil Co., 1938, 22 Del. Ch. 333, 2 A.2d 138, 37 U.S.P.Q. 834 11

Hall Laboratories v. National Aluminate Corp., 120 F.Supp. 684, 224 F.2d 303 13

Hardwick v. Gailbraith, 147 Pa. 333 ..... 11, 13

Hazeltine Research v. DeWald (1st Dept. 1950), 276 App. Div. 1001, 95 N.Y.S. 2d 772; 85 U.S.P.Q. 222, reversing 84 N.Y.S. 2d 597, 79 U.S.P.Q. 446 11

PAGE

Heath v. A. B. Dick Co., 253 F.2d 30 (C.A. 7, 1958) 10

Heller Inc. v. Lassner Co. (1st Dept. 1925), 214 App. Div. 315; 212 N.Y. Supp. 175 11

Hennessy v. Bacon, 137 U.S. 78, 85 (1890) 5

Jungersen v. Morris Kaysen (Pa. C.P. 1952) 95 U.S.P.Q. 162, aff'd 173 Pa. Super. 114, 97 U.S.P.Q. 244 (1953) 11, 13

Lehman Co. v. Appleton Toy & Furniture Co. (C.A. 7, 1945), 148 F.2d 988 13

Muth v. J. W. Speaker Corporation (C.A. 7, 1959), 262 F.2d 797, 801 16

Pope Mfg. Co. v. Owsley (C.C. N.D. Ill., 1886), 27 F. 100 13

St. Paul Plow Works v. Starling, 140 U.S. 184, 195, 35 L.Ed. 404, 407 (1891) 9

Universal Rim Co. v. Scott, N.D. Ohio E.D., 1922, 21 F.2d 346 12

Vicki Hosiery v. Margulies, E.D. Pa., 1958, 164 Fed. Supp. 738 12

Washburn & Moen Mfg. Co. v. Cincinnati Barbed-Wire Fence (C.C.S.D. Ohio, 1884), 22 Fed. 712 11

Williams v. First National Bank, 216 U.S. 582, 595 (1910) 5

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1959.

No. 890

BOWERS MANUFACTURING CO., INC.,

Petitioner,

vs.

ALL-STEEL EQUIPMENT INC.,

Respondent.

RESPONSE TO PETITION FOR WRIT OF CERTIORARI.

STATEMENT OF FACT.

By its decision below, the Court of Appeals for the Ninth Circuit affirmed the judgment of the District Court (R 114), which entered judgment against Petitioner in the amount of approximately $12,000.00 and by a mandatory injunction required Petitioner to make royalty reports and payments provided for in a patent license agreement between Petitioner and Respondent.

The judgment was based upon Findings of Fact and Conclusions of Law (R 110-114) finding that on January 1, 1955, Petitioner and Respondent entered into a nonexclusive patent license agreement by which Petitioner became obligated to pay royalties for its production and sale of cable clamps covered by Patent No. 2,424,829; that Petitioner had paid royalties under the agreement for a time but had ceased paying royalties, although it admitted it had produced cable clamps covered by Patent

No. 2,424,829; that the agreement was still in effect, and that royalties should be paid by Petitioner to Respondent. The Court concluded as a matter of law that Petitioner's attempt to terminate the agreement by a simple notice of termination was not legally sufficient to effectuate a termination.

A brief statement of the facts leading up to the execution of the license agreement and reference to a few pertinent terms of the agreement will facilitate an understanding of the simple principle of contract law which determines Petitioner's contractual liability.

Respondent, the owner of Patent No. 2,424,829 by letter (R 21) charged Petitioner with infringement of the patent, and by letter (R 23) Petitioner responded, stating that it had no deliberate intention to infringe. Petitioner subsequently (R 24) by letter conceded that the products made by it were fully covered by Respondent's patent and suggested a settlement of the controversy by the grant of a license. The parties by letters (R 25-28) negotiated the terms to be incorporated in the proposed license agreement, and an agreement (R 30) was submitted to Petitioner for execution. Further negotiations in the form of a letter (R 34) from Petitioner to Respondent occurred, and a revised agreement was submitted (R 36), which was accepted by Respondent.

The agreement provided for the grant of a non-exclusive license under Patent No. 2,424,829 to Petitioner, which license was to extend for the full term of the patent. Petitioner was to pay a royalty of one per cent of the net sale price of all switch and outlet boxes including cable clamps covered by Patent No. 2,424,829, with payments to be made yearly. A significant portion of the agreement provided that Petitioner should have the right to cancel

the non-exclusive license agreement only in the event that:

(a) The licensed patent was held invalid by a court of competent jurisdiction from which no appeal was taken; or

(b) Petitioner completely discontinued the manufacture and sale of boxes embodying cable clamps covered by Patent No. 2,424,829 (R 38).

Upon the execution of the license agreement, Petitioner paid to Respondent $1,108.00 as royalties for infringing production during 1954, and under the terms of the license Petitioner paid $3,594.00 as royalties for production during the year 1955.

Petitioner concedes (R 56-59, R 101-105) that during the years 1956, '57 and '58 it made and sold switch or outlet boxes including cable clamps covered by Patent No. 2,424,829 having a total sales price in excess of $1,107,000.00 upon which royalties were not paid. The royalty rate being one per cent, as provided in the agreement, the royalties approximate $11,000.00.

Upon Petitioner's continued refusal to submit royalty reports and make royalty payments, this action was commenced in the District Court to collect the amounts due under the license agreement and for specific performance to compel Petitioner to adhere to the terms of the license agreement. In the District Court, Petitioner pleaded termination of the license agreement by its unilateral notice of termination (R 81-84).

A motion was filed in the District Court to strike certain portions of Defendant's answer pleading unilateral termination, and to dismiss counterclaims for a declaration of invalidity and for recovery of royalties predicated solely upon the asserted termination. The District Court

held that the attempted termination or repudiation of the license agreement was not legally effected; that the defenses and counterclaims were therefore legally insufficient; and, finding (R 114) that Petitioner had no defense to the complaint other than that set forth in the stricken paragraphs, entered judgment.

There is no dispute as to any of the facts found by the District Court. The only question presented is a simple question of contract law.

QUESTION PRESENTED.

The question of law presented in the petition for certiorari should be stated as follows: May a nonexclusive licensee by a simple notice of termination effectively terminate a license agreement contrary to the terms thereof?

ARGUMENT.

The facts establish that when Petitioner conceded the infringement of Respondent's patent, prospective litigation was imminent. The parties in lieu of litigation compromised the controversy by the execution of the license agreement. Petitioner is not contending that any undue advantage was taken of it during the negotiations, and does not assert that the agreement was in any respect illegal. The agreement was legal when executed, and Petitioner's only excuse for repudiation was its after-acquired observation that the patent under which it had a nonexclusive license might be invalid. Such assumed invalidity is asserted to avoid its contractual obligation to pay royalties. Nevertheless, it is abundantly clear that the agreement between Petitioner and Respondent was executed to settle prospective patent litigation.

In *Williams* v. *First National Bank*, 216 U.S. 582, 595 (1910), this Court stated:

> "Compromises of disputed claims are favored by the courts * * *; and presumptively, the parties to the compromise in question possessed the right to thus adjust their differences. * *"

In a situation where one of the parties asserted that it had made a bad bargain this Court, in *Hennessy* v. *Bacon*, 137 U.S. 78, 85 (1890), stated:

> "* * * It was a case of the compromise of a disputed claim, the parties dealing with each other upon terms of perfect equality, holding no relations of trust or confidence to each other, and each having knowledge, or having the opportunity to acquire knowledge, of every fact bearing upon the question of the validity

> of their respective claims. • • • Such a settlement ought not to be overthrown, even if the court should now be of opinion that the party complaining of it surrendered rights that the law, if appealed to, would have sustained. • • •".

In *Automatic Radio Mfg. Co., Inc.* v. *Hazeltine Research, Inc.*, 176 F.2d 799, 806 (affirmed 339 U.S. 827), the Court of Appeals for the 1st Circuit stated:

> "• • • It is not uncommon for the parties to a patent infringement suit, in which there is a genuine issue as to the validity of the patent, to make a settlement of the litigation by an agreement under which the patentee gives a license to the alleged infringer in consideration of the payment of a stipulated royalty. Indeed, the license agreement in suit seems to have been by way of settlement of earlier litigation between the parties. It is not apparent to us that the public interest would be served by rendering such common-sense business settlements nugatory, which would be the result of a ruling that the licensee could reopen the issue of validity when sued for the stipulated royalty."

In its opinion below, the Court of Appeals in the instant case stated:

> "General policy considerations favoring settlement of disputes and litigation by means of such nonexclusive licenses should not allow a licensee to attack the validity of a licensor's patent by means of a device such as prior rescission, anymore than by direct attack through a suit for royalties. The licensee has bought temporary peace by agreeing to the license, and should be required to abide by his bargain. • • •"

Petitioner argues that the law should be that a nonexclusive licensee by simple unilateral notice of repudiation, because of alleged patent invalidity, may effectively

terminate a license agreement and thereafter in any suit on the contract plead invalidity of the patent.

By the nonexclusive license, Petitioner acquired only the right to be freed from a suit for patent infringement under the licensed patent. As a nonexclusive licensee, Petitioner did not acquire any monopoly or any exclusivity. After the grant of the license, Petitioner was still subject to competition in the sale of products covered by the licensed patent from Respondent and from any and all other companies whom Respondent might license. Petitioner argues that whenever it concluded that the licensed patent might be invalid it had the right to terminate the agreement because there was a failure of consideration.

It is important to note the difference between a nonexclusive and an exclusive license. This distinction was recognized by the Court of Appeals below when it stated:

> "* * * Whether it is exclusive or nonexclusive is usually ascertained by some chance remark of the court. Cases dealing with both types of licenses are cited indiscriminately. But logic would indicate that a different treatment is justified. The two types of agreements differ basically because the consideration inducing them differs in each. In an exclusive license the monopoly values of the patent loom large. The license is in effect a grant of the patent. But a nonexclusive license cannot eliminate competition. It constitutes little more than a shield from suit for infringement by the grantor. Thus questionable validity of the patent cannot constitute a failure of consideration."

In essence, the judgment of the District Court found that Petitioner's attempt at unilateral repudiation of the nonexclusive license agreement was ineffective to terminate the agreement; that the agreement was still in effect, and therefore Petitioner, a licensee, was estopped to contest

the validity of the licensed patent. Petitioner does not question the doctrine of licensee estoppel. Such a position would be directly contrary to the opinion of this Court in *Automatic Radio Mfg. Co., Inc.* v. *Hazeltine Research, Inc.*, 339 U.S. 827, wherein this Court stated:

> "• • • Finally it is contended that notwithstanding the licensing agreement, petitioner-licensee may contest the validity of the patents it is charged with using. The general rule is that the licensee under a patent license agreement may not challenge the validity of the licensed patent in a suit for royalties due under the contract. *United States* v. *Harvey Steel Co.*, 196 US 310, 49 L. ed 492, 25 S Ct 240. • • •"

In order for Petitioner to be in a position to challenge the validity of the licensed patent, it must effect a repudiation or termination of the license agreement. Unless the contract provides for termination by the licensee, there is no escape. The contract provided that it would run until the expiration of Patent No. 2,424,829, an event which does not occur until 1964.

Specific provisions permitting relief from the payment of royalties were included in the agreement, one of these being in the event that the patent was held invalid in third party litigation, and the other in the event that Petitioner ceased manufacturing any items covered by the patent in suit. The patent has never been held invalid in any third party litigation, and Petitioner concedes that it has continued the manufacture of switch or outlet boxes including cable clamps covered by the licensed patent.

Petitioner urges two grounds for the grant of certiorari. These grounds shall be hereinafter discussed under appropriate headings.

1. THE DECISION OF THE COURT OF APPEALS IN THIS CASE IS IN HARMONY WITH THE DECISION OF THIS COURT AND WITH THE DECISIONS OF OTHER COURTS OF APPEAL. THERE IS NO BASIC CONFLICT OF DECISION.

Petitioner urges that a nonexclusive licensee may be permitted by notice to terminate a license agreement entered into in settlement of a controversy, even where such attempted termination is contrary to the specific terms of the agreement.

In *St. Paul Plow Works* v. *Starling*, 140 U.S. 184, 195, 35 L.Ed. 404, 407 (1891), this Court stated:

> "* * * we are of opinion that the circuit court was correct in holding that the defendant could not terminate, without the consent of the plaintiff, the rights conferred by the license, and that, as there was no limitation on its face, the license continued until the expiration of the patent. The contract has no provision for its termination or its renunciation.
>
> * * *
>
> "We are of opinion that the license, in the absence of a stipulation providing for its revocation, was not revocable by the defendant, except by mutual consent or by the fault of the other party. * * *
>
> "The defendant could not coerce the plaintiff into putting an end to the contract, by the means it adopted. * * *"

In *Automatic Radio Mfg. Co.* v. *Hazeltine Research, Inc.*, 176 F.2d 799 (C.A. 1, 1949; affirmed 339 U.S. 827), the Court of Appeals for the 1st Circuit stated:

> "* * * In addition to that, so far as it may be a question of federal law, in the absence of a cancellation option in the agreement, or of a substantial default by the licensor, the licensee cannot by any such unilateral notice of repudiation terminate its contract

obligation under a license agreement having several years yet to run. *St. Paul Plow Works* v. *Starling*, 1891, 140 U.S. 184, 11 S.Ct. 803, 35 L.Ed. 404; * * * (page 809)

In *Heath* v. *A. B. Dick Co.*, 253 F.2d 30 (C.A. 7, 1958), the Court of Appeals for the 7th Circuit stated:

"* * * The execution of the license agreement and the subsequent payment of royalties thereunder for about five years indicate that defendant, fully aware of its legal rights and on its own initiative, procured from plaintiff the right to make and market its stencil assembly. Defendant makes no charge of deception, fraud, or coercion on the part of plaintiff surrounding the execution of the agreement. Defendant's general counsel was evidently convinced that, to avoid liability as an infringer, or at least to avoid litigation involving a charge of infringement, it was good business for defendant to procure the license in question. By so doing, defendant became free to produce its assembly without fear of litigation with plaintiff. When it procured the license from plaintiff, defendant bought its peace. That it would thus serve the interests of defendant, was undoubtedly its best judgment. About five years later one of defendant's officers took a different view and decided that defendant did not need and never had needed a license from plaintiff. Upon his determination of what was good for defendant then, as well as in 1948, defendant undertook to cancel an agreement which contained no express right of cancellation and which, by its terms, was not to expire until the expiration of the patent. The question as to whether defendant actually needed the license in 1948 was one for it to determine at that time. By its general counsel it expressed such determination in 1948, and, as a result, had freedom from litigation and the use of license rights for five years before someone in its organization decided, in effect that it had never needed a license from plaintiff. If a person decides

that he needs a brown hat and he thereupon goes to a store and buys it, pays for it and wears it, no one would make the absurd contention that he would have a right to refuse to pay for the hat, or, if he had already paid for it, to recover the purchase price from the store owner because he had since decided that he did not need the hat and had not needed it when he bought it. We cannot sustain the defense based upon the 1953 decision of one of defendant's officers that defendant never had any need for the license which it asked for and procured from plaintiff in 1948."

There are many cases to the same effect, some of them being as follows:

Washburn & Moen Mfg. Co. v. *Cincinnati Barbed-Wire Fence*, C.C.S.D. Ohio, 1884, 22 Fed. 712;

Dall Motor Parts Co. v. *Packard*, 1931, 124 Ohio St. 363, 178 N.Ed. 835, 12 U.S.P.Q. 185;

Eastern States Petroleum Co. v. *Universal Oil Co.*, 1938, 22 Del. Ch. 333, 2 A. 2d 138, 37 U.S.P.Q. 834;

Heller Inc. v. *Lassner Co.* (1st Dept. 1925), 214 App. Div. 315; 212 N.Y. Supp. 175;

Hazeltine Research v. *DeWald* (1st Dept. 1950), 276 App. Div. 1001, 95 N.Y.S. 2d 772; 85 U.S.P.Q. 222, reversing 84 N.Y.S. 2d 597, 79 U.S.P.Q. 446;

Jungersen v. *Morris Kaysen* (Pa. C.P. 1952), 95 U.S.P.Q. 162, aff'd 173 Pa. Super. 114, 97 U.S.P.Q. 244 (1953);

Hardwick v. *Gailbraith*, 147 Pa. 333;

Air King Products Co. v. *Hazeltine Research*, E.D. N.Y. 1950, 94 Fed. Supp. 85, 87 U.S.P.Q. 315.

The only cases which seem to depart from the well established rule that a nonexclusive licensee may not repudiate his contract by unilateral notice are *Universal Rim Co.* v. *Scott*, N.D. Ohio E.D., 1922, 21 F.2d 346, and *Vicki Hosiery* v. *Margulies*, E.D. Pa., 1958, 164 Fed. Supp. 738. Both of these District Court cases were considered by the Court of Appeals below, and the Court pointed out that the *Universal Rim* Case is complicated by the intervention of a receivership and the rights of the receiver with respect to an executory contract. The Court below characterized the *Vicki* Case as being a decision rendered during the pleading stage of the case and did not enter into any discussion with respect to the substantive law here in issue. It thus appears that the opinion of the Court below is completely consistent with an earlier decision of this Court and with Courts of Appeal for other circuits.

Petitioner refers to an apparent conflict of authorities on a somewhat related question but limited to exclusive licenses. Whether or not a licensee under an *exclusive* license may terminate the license agreement upon the assertion of invalidity of a patent seems by the cases to be in doubt, but conflict of authority with respect to *exclusive* licenses cannot be resolved by this petition since in this case only a *nonexclusive* license is involved. The Court below, as indicated earlier, was well aware of the difference in effect between a nonexclusive and an exclusive license.

If Petitioner's proposition of law is sound that a nonexclusive licensee, upon receiving an opinion from its patent lawyer that the licensed patent is invalid, may by notice terminate the license agreement, then certainly such a licensee may, upon an adjudicated holding of invalidity, terminate such a license. In the first instance, the invalidity is merely suggested but the actual fact is

in doubt. In the second case, the speculation has been somewhat removed by the formal court adjudication of invalidity. It has repeatedly been held that a formal adjudication of invalidity, in the absence of contract provisions to the contrary, does not excuse a licensee from the payment of royalties, and such adjudicated invalidity does not constitute a failure of consideration for the license.

Pope Mfg. Co. v. *Owsley* (C.C. N.D. Ill., 1886), 27 F. 100;
Hardwick v. *Gailbraith*, 147 Pa. 333;
Jungersen v. *Kaysen* (Pa. C.P. 1952), 95 U.S.P.Q. 162;
Lehman Co. v. *Appleton Toy & Furniture Co.*, (C.A. 7, 1945), 148 F.2d 988;
Hall Laboratories v. *National Aluminate Corp.*, 120 F. Supp. 684, 224 F.2d 303.

With the exception of the two District Court cases relied upon by Petitioner, which may be distinguished for the reasons given in the opinion of the Court of Appeals below, the law is uniformly established by this court, by the decisions of other courts of appeal, and followed by the decision below, that a nonexclusive licensee may not, in the absence of contract provisions to the contrary, repudiate and terminate by notice the license agreement and attempt to avoid the payment of royalties merely upon a suggestion that the licensed patent is invalid. It may not even do so where the patent has been formally adjudicated to be invalid.

2. THE OPINION BELOW IS NOT IN CONFLICT WITH APPLICABLE STATE LAW.

Petitioner urges that Section 1689 of the California Civil Code is pertinent to the present litigation, and that

the decision below is in conflict with this statute and with applicable California decisions. The provisions of the Code referred to by Petitioner are Sections 3 and 4, which permit termination of a contract if the consideration becomes void or fails in any material respect. This section of the California Code cannot be applicable to the agreement between the parties here because Petitioner has always received what it bargained for—the right to be freed from a suit for patent infringement.

The authorities hold that even an adjudication of invalidity of a patent is no basis for the nonpayment of royalties by a nonexclusive licensee, and that such adjudication does not work a failure of consideration to the nonexclusive licensee. This is for the reason that he was not bargaining for exclusivity.

Petitioner refers to the California case of *Armstrong* v. *Shell*, 98 Cal. App. 769. The opinion of the Court of Appeals below is not in conflict with this California case, because to the extent that the California case referred to the right of a licensee to repudiate a license the opinion was dicta; and, furthermore, as to this portion of the case one of the three judges specifically refused to concur and another of the three judges dissented from the whole of the opinion.

It is submitted that the later case of *Del Riccio et al.* v. *Photochart*, decided by the California District Court of Appeals in 1954, establishes the applicable California law, and is in harmony with the Court of Appeals below. In its opinion in the *Del Riccio* Case, the California District Court of Appeals stated:

> "• • • Appellant argues that this finding is directly contrary to the only evidence in the record relative to eviction, and which, it is contended, shows con-

clusively that after the aforesaid federal court decision, appellant's licensees refused to make payments for use of an invalidated patent, and that competitors were invading the field formerly denied to them. While it appears to be the law that where an *exclusive* license is granted and the patent is held invalid by the courts, the licensee may successfully claim an eviction, the argument is inapplicable where as here, the license is nonexclusive. * * *" (268 P. 2d 814)

There is thus no conflict with either the California statute or the applicable California law.

CONCLUSION.

It is suggested that the Court of Appeals below is in error in its opinion and that this Court should have an opportunity to correct such error. The decision of the Court below is in harmony with the *St. Paul Plow Works* case decided by this Court, and is in harmony with the opinions of other Courts of Appeal on the identical question. Independently of the numerous decisions establishing the law as followed by the Court below, reason dictates such a conclusion. It would violate fundamental legal concepts to permit a party to a license agreement to avoid the payment of royalties simply because of its assertion of invalidity of the patent under which it has a nonexclusive license. This is particularly true where the nonexclusive license agreement was entered into in settlement of prospective patent litigation.

By its agreement obtained after negotiation and at arm's length dealing, Petitioner acquired freedom from a suit for patent infringement at a price. It got, and still has, what it bargained for.

As stated in *Muth* v. *J. W. Speaker Corporation* (C.A. 7, 1959), 262 F.2d 797, 801:

> "Defendant throughout its brief suggests that it might be contrary to public policy to make it pay a royalty where others would make the same device without such payment. However, it is not definitely known whether another would make the device without running the risk of an infringement suit. The question apparently concerned defendant also and it led to the agreement in question. The defendant chose to buy immunity from lawsuits, justified or otherwise, at a certain price. It got just what it paid for. To allow defendant to renege on its agreement simply because it may now feel that it was overcautious would certainly be more incompatible with public policy."

The case below presents a simple question of contract law. It was decided correctly by the District Court and by the Court of Appeals in a decision which gives consideration to all of the arguments presented here by the Petitioner. There is presented in the petition no issue of major significance requiring the consideration of this Court.

Under these circumstances, it is urged that the petition for certiorari be denied.

Respectfully submitted,

THOMAS F. MCWILLIAMS,
Attorney for Respondent.

Chicago, Illinois
May 19, 1960